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SUBJECT: Austria's Economic Outlook - Deep Recession in 2009,
Stagnation in 2010

REF: (A) VIENNA 0615; (B) VIENNA 0402

¶1. SUMMARY: After a dismal first quarter, Austria is confronting a deeper recession than projected earlier this year. As a result, Austria's two leading economic institutes have downgraded their GDP growth forecasts for 2009 (contraction of 3.4-4.3%) and 2010 (stagnation). Austria's recession is severe, persistent, and widespread. Unemployment will rise to 5.3-5.4% in 2009 and about 6% in 2010. The budget deficit will rise sharply to about 4.4%/GDP in 2009 and 5.4-5.8%/GSP in 2010. END SUMMARY.

Miserable First Quarter Means Deeper Recession

¶2. Austria's economy contracted 2.8% in Q1/2009 (versus Q4/2008) on the back of rapidly falling exports and investments; the contraction was steeper than expected (ref A), pulling down 2009 and 2010 forecasts. Private consumption remains the only meager stabilizer. The Austrian Institute for Economic Research (WIFO) expects some improvement in Q2/2009, while the Institute for Advanced Studies (IHS) is more pessimistic. WIFO cut its growth forecast for 2009 (by 1.2%/GDP) to -3.4%; IHS cut its 2009 forecast (by 1.6%) to -4.3%. Despite early indications that the Austrian economy could bottom out in mid-2009, economists are not raising any hopes. WIFO Director Karl Aiginger characterized the situation as unstable, with financing and liquidity problems which justify continued GoA stimulus measures. IHS Director Bernhard Felderer expects a miserable second quarter, followed by stabilization towards the end of the year.

¶3. Forecasters see goods exports declining in 2009 by around 15% (real terms), imports (10%), investment (6-9%), with private consumption essentially flat and public consumption growing by 0.5%. Inflation is not on the horizon: combined with the GoA's recent income tax cut, this means that real after-tax incomes (per capita) will rise 3.3% in 2009. The savings rate will rise to 12% of disposable income in 2009 from 11.5% in 2008.

Stagnation in 2010

¶4. Austria's economic institutes see the downward trend flattening in the second half of 2009 and the economy essentially stagnating in 2010 (WIFO expects growth of 0.5%, IHS 0.3%). Exports and imports of goods are expected to grow modestly and private consumption should grow by 0.2-0.5% (public consumption by 0.8-1.5%), while investment will shrink by a further 1-2%. CPI inflation will remain moderate at 1.2-1.6%. With meager wage increases and rising inflation, real per capita after-tax incomes will shrink 0.3% in 2010. The savings rate is expected to fall slightly to 11.3-11.7%.

Assumptions for Growth Forecasts

15. The institutes base their revised 2009/2010 forecasts on the following assumptions:
 -- U.S. economic growth of -2.7% to -2.8% in 2009 and 0.5-1.5% in 2010;
 -- Euro-zone growth of -4.2% to -4.5% in 2009 and 0.3% in 2010;
 -- EU-27 growth of -4.0% in 2009 and 0.3-0.5% in 2010;
 -- German economic growth of -6.0% in 2009 and 0.5% in 2010;
 -- Average oil prices of \$60-61 per barrel in 2009 and \$75 in 2010;
 and
 -- Average dollar/Euro exchange rates of 0.69-0.75 in 2009 and 0.69-0.77 in 2010 (i.e. little moment).

Labor Market Downturn, Strong Rise in Unemployment

16. Economists forecast average unemployment rates of 5.3-5.4% in 2009 and 5.8-6.3% in 2010, with little relief in 2011. Since the beginning of the year, the number of unemployed in Austria has risen strongly. In May, it was 30% higher than a year earlier (NOTE: 2008 was a banner year, with employment growth of 2.4%). In 2009, economists project employment to shrink 1.0-1.5% and the number of unemployed to rise by about 30% or 60,000-70,000 for an annual average of close to 280,000 unemployed. For 2010, the institutes project employment to shrink by another 1.0% and the number of unemployed to rise by 15% or 40,000 for an annual average of 310,000-320,000. At 6.3%, the 2010 unemployment rate would be the highest in Austria since 1953, albeit at a much higher level of employment. In addition to those included in the unemployment statistics, Austria will have an additional 100,000 workers on furlough status / reduced working hours and in training.

Budget Deficit to Exceed 4% of GDP

17. Because of the GoA's large economic stimulus measures, the bank rescue package, and automatic stabilizers, WIFO and IHS now project a total public sector deficit of 4.3-4.4% in 2009 and 5.4-5.8% in 2010. As a result, public sector debt will swell from 59.4%/GDP in 2007 and 62.5%/GDP in 2008 to around 80%/GDP by 2011. Aiginger and Felderer agree on the necessity to reduce debt after the crisis, but think 2011 will be the first chance to introduce consolidation measures. At a July 8 press conference, IHS head Felderer (in his function as head of the Federal Debt Committee) advocated decisive cuts (starting in 2011) to reduce debt to 60%/GDP in line with the EMU's Maastricht criteria. However, even assuming 4% nominal growth (about 2% real growth) and an annual public sector deficit of 1%/GDP, it will take Austria at least 10 years to bring its debt level down again to 60%/GDP. Felderer sees the 80%/GDP level as costly, unsustainable, and detrimental for GoA creditworthiness and Austria as a business location.

18. Statistical Annex

Projections of Austrian Economic Indicators (percent change from previous year, unless otherwise stated)

	WIFO 2009	IHS 2009	WIFO 2010	IHS 2010
REAL TERMS:				
GDP	-3.4	-4.3	0.5	0.3
Manufacturing	-10.0	n/a	0.0	n/a
Private consumption	0.2	-0.2	0.5	0.2
Public consumption	0.5	0.8	1.5	0.8
Investment	-8.4	-9.4	-1.3	-2.1
Exports of goods	-15.1	-14.0	0.7	2.5
Imports of goods	-11.2	-9.5	0.4	1.5
Nominal EUR billion:				
GDP	277.0	274.1	280.8	277.6
Other indices:				
GDP deflator	1.6	1.4	0.9	1.0
Consumer prices	0.5	0.6	1.2	1.6
Unemployment rate	5.3	5.4	5.8	6.3

Current account (in percent of GDP)	0.8	n/a	0.9	n/a
Exchange rate (EUR / US\$ 1)	0.69	0.75	0.69	0.77

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